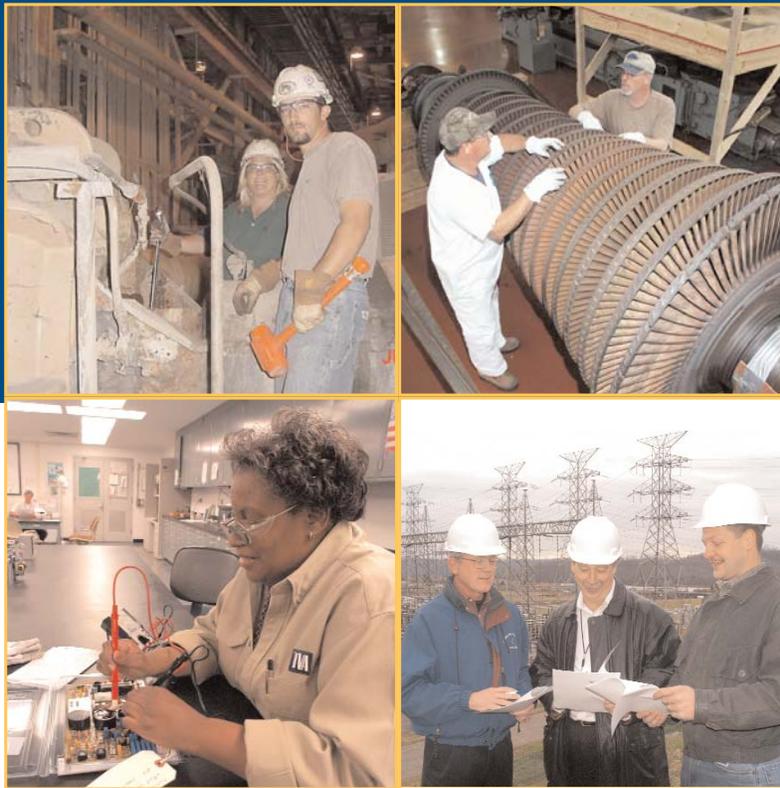


*S e m i a n n u a l R e p o r t*  
Office of the Inspector General



**April 1 ~ September 30, 2004**



The Office of the Inspector General (OIG) is an independent organization charged with reporting to the Tennessee Valley Authority (TVA) Board of Directors and Congress on the overall efficiency, effectiveness, and economy of TVA programs and operations. The OIG meets this responsibility by conducting audits, investigations, and other reviews.

The OIG focuses on the prevention, identification, and elimination of (1) waste, fraud, and abuse; (2) violations of laws, rules, or regulations; and (3) inefficiencies in TVA programs and operations.

If you want to report any matter involving TVA programs, operations, or employees, you should call the OIG Hotline or write the Inspector General's office at the address or number listed on the back cover.



# Tennessee Valley Authority Office of the Inspector General

## Message From the Inspector General

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This semiannual report summarizes the work of the OIG from April 1 through September 30, 2004. The audits, investigations, and inspections highlighted in this report illustrate our continuing commitment to helping TVA promote economy, efficiency, and effectiveness in its programs and operations.

During the past six months, our audits, investigations, and inspections continued to add to TVA's "bottom line." We identified over \$4.8 million in potential savings or recoveries, and TVA used our findings from this and prior reporting periods to save over \$7 million. The amount of realized savings illustrates how effectively the OIG and TVA work together both in identifying potential problems and resolving those problems. I appreciate the cooperation and support we receive from the TVA Board, management, and employees in our work.

As part of our efforts to focus our resources on major areas, we increased our manpower devoted to the Browns Ferry Nuclear Plant (BFN) Unit 1 Restart Project. Audit, investigation, and inspection resources are being dedicated to BFN to conduct reviews designed to promote cost control and to identify on a proactive basis fraud, waste, or abuse that may be occurring. We also have numerous projects underway to ensure integrity in our contract administration process and to look for cost savings opportunities. As an example, during this reporting period we determined, among other things, that a contractor providing engineering services for the BFN Unit 1 restart had overbilled TVA \$602,611. We will continue to examine the major contracts and subcontracts to ensure TVA is getting the benefit of its bargain.

Finally, I note that the OIG is losing one of its founding fathers. G. Donald Hickman, one of the first people to start this office in 1986, has retired. Mr. Hickman was the Acting Inspector General (IG) before my appointment and the Assistant Inspector General for Investigations for ten years. He has been heralded throughout the IG community for his work—in 2000 he received an Award of Excellence from the IG community, and this year he received an Individual Accomplishment Award for his work on the OIG investigation peer review process. Mr. Hickman's contributions to both the IG community and to the TVA OIG will be long remembered. He has our best wishes for a well-deserved retirement.

It is truly an honor to work alongside the many dedicated men and women who pull together to make TVA successful. They are aided, as are we, by the continued leadership and support of the TVA Board and the United States Congress. Together we can build a better TVA for future generations.

Richard W. Moore  
Inspector General  
October 29, 2004



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## Executive Summary

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During this reporting period, we continued to support TVA by conducting objective audits, investigations, and inspections. In accordance with our mission, our reviews are designed to promote economy, effectiveness, and efficiency while detecting and preventing fraud, waste, and abuse. In total, we identified over \$4.8 million in recoveries, fines/penalties, potential savings, questioned costs, or funds which could be put to better use, as outlined in the chart below.

<b>STATISTICAL HIGHLIGHTS</b>	
<b>April 1 ~ September 30, 2004</b>	
Audit Reports Issued	34
Questioned Costs	\$1,763,000
Funds Recovered/Disallowed	\$4,061,000
Funds Put to Better Use	\$1,471,000
Funds Released by TVA	\$7,196,000
Investigations Opened	118
Investigations Closed	163
Fines/Recoveries/Restitution/Savings	\$1,359,349
Criminal Actions	12
Administrative Actions (No. of Subjects)	30
Inspections Completed	8
Cost Savings	\$226,000

Our 34 audits and 8 other audit-related projects during this reporting period resulted in significant questioned costs and the identification of areas for improvement. Highlights for this semiannual period included the identification of (1) almost \$1.8 million in questioned costs and almost \$1.5 million in funds which could be put to better use from our contract audits, (2) needed improvements in the area of information technology (IT) security, (3) recommended improvements in future power generation decisions, and (4) enhanced controls for TVA's hospitality program. We also noted many positives in TVA activities. For example, we found no instances where TVA's external auditor did not comply with Government Auditing Standards in all material respects, and we determined TVA's IT security program structure is adequate to meet federal requirements and TVA is making substantial progress in correcting IT security deficiencies.



We also devoted additional resources to the restart of BFN Unit 1. Because of the significance and cost of the restart effort, we are committing audit, investigation, and inspection resources to ensure integrity in our contract administration process and to identify potential cost savings at BFN.

We continued our focus on developing a comprehensive approach to detecting and preventing fraud and waste. Our actions, which complement the Sarbanes-Oxley Act, which does not generally apply to TVA, include creating a data mining program and an intelligence and analysis unit and initiating training to conduct fraud risk assessments throughout TVA.

Investigative highlights include (1) recoveries, savings, and fines/penalties which exceed \$1.3 million, (2) per diem and workers' compensation fraud cases, (3) cases involving problems with coal sampling, and (4) credit card abuse cases, including purchasing cards, gas cards, and travel cards. For example, one TVA employee used his TVA purchasing card to purchase overpriced janitorial supplies in quantities far in excess of what TVA needed. In return, he received about \$14,500 in store gift cards and merchandise. We estimated TVA's loss to be between \$200,000 and \$400,000.

Our Inspections unit completed eight projects which identified over \$226,000 in cost savings and identified opportunities for improved program operations. Highlights include (1) a contract review which identified \$204,229 in overbillings and (2) a review of one contractor under TVA's energy right® program. The latter review found the contractor engaged in various improper schemes and identified numerous opportunities for improvement in TVA's internal controls over the program.

## Definitions

**Questioned Costs** - A cost that is unnecessary, unreasonable, unsupported, or an alleged violation of law, regulation, contract, etc.

**Unsupported Costs** - A questioned cost that is not supported by adequate documentation.

**Funds Put to Better Use** - Funds that could be used more efficiently by implementing recommended actions.

**Disallowed Costs** - A cost that management agrees should not be charged to TVA.



## TVA Profile

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TVA was created during 1933. President Franklin Roosevelt asked Congress to create “a corporation clothed with the power of government but possessed of the flexibility



and initiative of a private enterprise.” On May 18, 1933, Congress passed the TVA Act, creating TVA as a federal corporation whose primary purposes are to provide flood control, navigation, and electric power in the Tennessee Valley region.

Today TVA is the nation’s largest public power company. TVA’s power facilities include 11 fossil plants, 29 hydroelectric dams, 3 nuclear plants, 6 combustion turbine plants, a pumped-storage facility, and 17,000 miles of transmission lines. TVA also produces energy from three renewable sources—sun, wind, and methane gas from waste. The TVA service area covers 80,000 square miles in the Southeastern United States, including almost all of Tennessee and parts of Mississippi, Kentucky, Alabama, Georgia, North Carolina, and Virginia. By providing wholesale power to 158 municipal and cooperative power distributors, and by directly serving 62 large industries and government installations in the Valley, TVA supplies the energy needs of 8.5 million people.

As a regional development agency, TVA not only supplies affordable, reliable power, but also supports a thriving river system and stimulates sustainable economic development in the public interest. TVA manages the nation’s fifth largest river system. TVA dams are part of a totally integrated resource management system where each dam operates in relationship to the others for multiple purposes and public benefits, including flooding, maintaining navigation, providing recreational opportunities, and protecting water quality in the 41,000-square-mile watershed.

TVA contributes to the Valley economy chiefly by keeping power rates competitive, which helps attract and retain industries that provide quality jobs in the region. TVA also helps communities promote sustainable economic development by providing assistance in job creation and retention and productivity improvements via capital investment, support of business incubators, specialized technical services and advice, and recruitment for new and existing industries.



## Office Authority

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Created by the TVA Board of Directors during 1985, the TVA OIG became statutory under the IG Act Amendments of 1988. The authority to appoint the TVA IG was transferred to the President in November 2000 by Public Law No. 106-422.

The IG is responsible for conducting audits and investigations relating to TVA programs and operations while keeping the TVA Board and Congress fully and currently informed about problems and deficiencies. The TVA IG is independent of TVA management and subject only to the general supervision of the TVA Board. The IG's authority includes conducting audits or investigations the IG deems necessary or desirable, issuing subpoenas, administering oaths, and granting confidentiality to individuals who provide information to the OIG.

## Organization

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The OIG's primary location is in the TVA headquarters in Knoxville, Tennessee. To obtain broader coverage throughout the Valley, the OIG also has an Inspections unit located in Chattanooga, Tennessee, and one-person offices at BFN in Alabama and in Mayfield, Kentucky. During this reporting period, the OIG consisted of three primary components: Audits, Investigations, and Inspections.



### AUDIT OPERATIONS

Audit Operations (AO) conducts and/or supervises comprehensive financial and



performance audits of TVA programs and operations and makes recommendations to ensure that program objectives and operational functions are achieved effectively and efficiently. AO develops an annual audit plan to enable effective allocations of audit resources to issues, programs, operations, and activities that expose TVA to significant risks and/or vulnerabilities.

AO consists of three departments—Contract Audits, Financial/Operational Audits, and IT Audits.

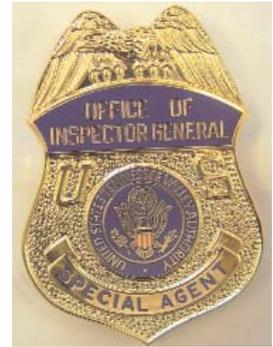
- Contract Audits has lead responsibility for contract compliance and preaward audits. In addition, this group performs reviews of TVA contracting processes and provides claims assistance and litigation support.
- Financial/Operational Audits has lead responsibility for (1) oversight of TVA's financial statement audits performed by TVA's external auditor; (2) reviews of TVA's internal controls related to financial reporting, operational efficiency, and compliance with laws and regulations; and (3) operational reviews to assess the results and economy and efficiency of TVA programs.
- IT Audits has lead responsibility for audits relating to the security of TVA's IT infrastructure, application controls, and general controls associated with TVA systems. This group also performs operational reviews of the effectiveness of IT-related functions. In addition to its audit mission, IT Audits is responsible for developing and supporting an independent OIG computer network.

AO refers possible fraud or other wrongdoing by contractors, employees, or others identified during its audits to Investigative Operations for further review. As needed, AO also provides data mining and other assistance to, or performs joint projects with, the Inspections and Investigations units.



## INVESTIGATIVE OPERATIONS

Investigative Operations (IO) conducts and coordinates investigative activity related to fraud, waste, and abuse in TVA programs and operations. The activities investigated include possible wrongdoing by contractors, employees, economic development loan recipients, and others. IO maintains liaisons with federal and state prosecutors, and reports to the Department of Justice whenever the OIG has reasonable grounds to believe there has been a violation of federal criminal law. IO works with other investigative agencies and organizations on special projects and assignments, including interagency law enforcement task forces on terrorism, the environment, and health care.

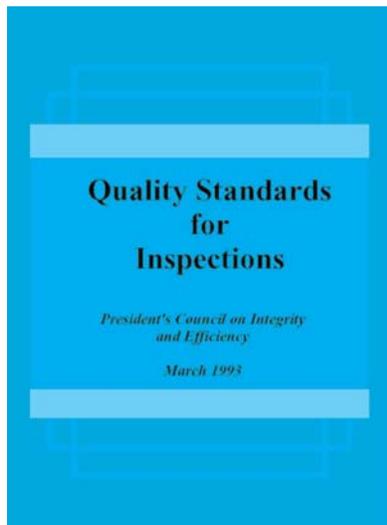




### INSPECTIONS

The Inspections unit, which is staffed by auditors and investigators, was formed at the beginning of fiscal year (FY) 2004. Inspections provides flexibility to conduct quick hit policy and program evaluations to promote economy and efficiency in the management and administration of TVA programs and to prevent and detect fraud, waste, and abuse. In accordance with the Quality Standards for Inspections, the objectives of inspections include providing a source of factual and analytical information, monitoring compliance, measuring performance, assessing the efficiency and effectiveness of operations, and/or conducting inquiries into allegations of fraud, waste, abuse, and mismanagement.

During this period, Charles A. Kandt, Assistant Inspector General for Inspections and a reservist, was serving on active duty in the Middle East. Mr. Kandt is a Lieutenant Colonel in the Army Reserves and has been a JAG officer for 23 years. During his absence, Ben R. Wagner, Assistant Inspector General for Audits, has served a dual role in heading up both Audits and Inspections.





**NEW ASSISTANT INSPECTOR GENERAL FOR ADMINISTRATION AND GOVERNMENT RELATIONS**

During this reporting period, we created a new position, Assistant Inspector General for Administration and Government Relations (AIGAGR), to oversee our administrative function and make us more cognizant of what is occurring in the congressional area.

Ronald Wise is our first AIGAGR. Before becoming the AIGAGR, Mr. Wise was an Assistant United States Attorney in the Southern District of Alabama. Mr. Wise's background also includes being a trial attorney in the General Counsel's Office, United States Navy.



By creating this new position, we will be able to enhance office administration, staffing and retention practices, and develop working relationships with congressional members and ensure we keep them informed of our activities and are responsive to their concerns. Mr. Wise will be coordinating with various stakeholders, including members of the TVA Caucus and TVA's Government Relations organization.

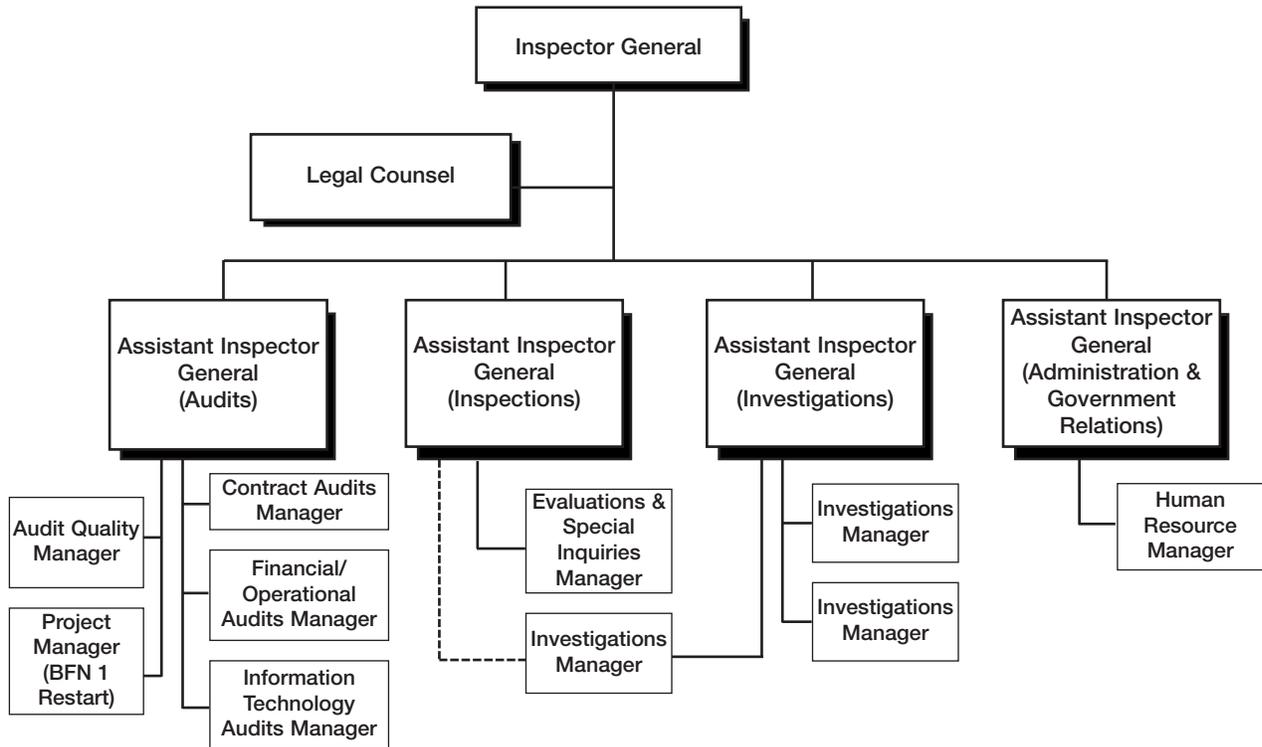
**NEW ASSISTANT INSPECTOR GENERAL FOR INVESTIGATIONS**

G. Donald Hickman, Assistant Inspector General for Investigations for the past ten years, retired at the end of this reporting period. He will be replaced by Charles A. Kandt, who will serve as both the Assistant Inspector General for Inspections and the Assistant Inspector General for Investigations. Before coming to the OIG, Mr. Kandt was an Assistant United States Attorney for the Southern District of Alabama, where he worked with law enforcement agencies through the Organized Crime Drug Enforcement Task Force and handled criminal appeals.





# Office of the Inspector General



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**Hotline to report fraud, waste, and abuse: 1-800-323-3835**  
**OIG website: <http://oig.tva.gov>**



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### OIG Increases Oversight of the BFN Unit 1 Restart Project

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In May 2002, the TVA Board of Directors approved a plan to return BFN Unit 1 to service. BFN Unit 1, which began commercial operation on August 1, 1974, has not operated since 1985. However, a study conducted by TVA during 2001 determined BFN Unit 1 could be returned to service “safely and economically.” TVA estimated the restart project would cost \$1.8 billion over a five-year period.

To complete the restart of BFN Unit 1, TVA contracted with Bechtel Power Corporation (for design engineering services) and Stone and Webster Construction, Inc. (for construction modifications). TVA has estimated about 4.5 million workhours will be required to complete the engineering scope of work, and about 12 million workhours will be required to complete the modifications. Additionally, General Electric will be providing equipment and services needed for the modifications.

As a result of the significance of this project, the OIG has increased its oversight effort. We have permanently assigned an auditor and an investigator to the BFN location in Decatur, Alabama, and have completed a comprehensive survey to identify and prioritize areas to concentrate our reviews. We are using audit, inspection, and investigative resources to conduct reviews designed to promote cost control and to identify on a proactive basis any fraud, waste, or abuse. We also have many projects underway to ensure integrity in our contract administration processes and to look for cost savings opportunities.



Our efforts in connection with the BFN restart during the past six months have included the following:

- We determined a contractor providing engineering services for the recovery of BFN Unit 1 overbilled TVA \$602,611. Specifically, the contractor billed TVA for (1) certain home office labor that was already recovered in its overhead rate, (2) unsupported



## Special Features

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and ineligible costs and fees related to a subcontract agreement with an affiliated company, (3) ineligible and unsupported computer charges, (4) casual employee labor, and (5) other direct costs that had already been recovered through a separate billing rate. TVA management is reviewing the audit issues to determine the actions it should take. Additionally, we have ongoing contract audits on the major contractors at BFN. We are reviewing subcontractors as well.

- Our audit of BFN contractors' willingness to report nuclear safety and quality issues showed they generally felt free to raise nuclear safety and quality issues through some avenue.
- Our inspection of the Consignment Inventory Payment controls determined that controls could be strengthened by (1) updating the current guidelines, (2) providing additional training for those responsible for controls, (3) strengthening the process of maintaining and verifying pricing information, (4) initiating management review of usage reports to ensure reasonableness and appropriateness of materials purchased, and (5) establishing controls surrounding the materials requisition forms. TVA management agreed to implement all the recommendations.
- We closed six investigations during this reporting period. While most of those investigations did not find wrongdoing, in one per diem investigation we determined a contract employee filed a certification containing a false statement in order to obtain \$12,332 in per diem. The contract employee died prior to completion of the investigation, and management recovered the payments from the contractor.

We also had two cases with indictments related to BFN.

- In a joint investigation with the United States Postal Service, we found an employee at BFN misused his TVA purchasing card by accepting kickbacks to purchase overpriced janitorial supplies in quantities far in excess of what TVA needed. In return, the former employee received about \$14,500 in store gift cards and merchandise. The former employee and a co-conspirator have been indicted on 21 counts,





including conspiracy and wire fraud. The loss to TVA is estimated to be between \$200,000 and \$400,000.

- In the other case, a contract employee at BFN and members of her family used a TVA Wright Express Card for personal purchases totaling about \$10,000. The contract employee was indicted on four counts of felony theft.

### OIG Works With TVA on Initiative to Detect and Prevent Fraud

During this reporting period, we continued our focus on developing a comprehensive approach to detecting and preventing fraud and waste. In addition to assigning investigators as “road agents” to serve as key contacts at specific TVA facilities and referring more administrative allegations to management for resolution, as we reported in our last semiannual, we expanded our program in several areas.



While TVA management has the ultimate responsibility for fraud detection and prevention, our goal is to help TVA improve their antifraud processes and internal controls, while at the same time maintaining an effective oversight process and detecting and seeking prosecution of fraud where it exists. These actions complement the assessment of internal control over financial reporting by TVA management, including controls related to the prevention, identification, and detection of fraud. We will be working closely with TVA management in this initiative, and we expect that over time this program will produce significant results and will serve as a strong deterrent against fraud.

### **BACKGROUND**

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In response to a series of corporate scandals, Congress enacted the Sarbanes-Oxley Act in 2002. That law and the implementing regulations are intended to provide greater transparency in corporate accounting and reporting, provide greater accountability by making board members and executives personally responsible for financial statements, and place greater emphasis and structure around efforts to prevent, detect, investigate



## Special Features

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and remediate fraud and misconduct. Under this law, management is responsible for establishing, validating, and monitoring effective internal controls over fraud. Although TVA generally is not covered by the terms of Sarbanes-Oxley, it has determined that adopting procedures consistent with certain provisions of that Act will better assure any potential TVA investors and other key stakeholders that TVA is providing complete, accurate, and timely information about TVA.

The elements of a strong program to detect and deter fraud include sponsorship by upper-level management, assessments to identify fraud risks and controls which mitigate those risks, evaluations of the effectiveness of those controls, addressing residual risks, responding to suspicions of fraud, and taking remedial action to prevent recurrences where fraud is identified. TVA has taken initial steps to establish such a program. For example, the TVA Board has adopted a Code of Ethics and created a Disclosure Control Committee, and TVA has a fairly rigorous program to conduct background investigations on key managers and Nuclear employees. In addition, we have agreed to publicize the OIG Hotline as an avenue to report suspected financial and other types of fraud, and the OIG has a documented process for receiving and investigating complaints.

We believe, however, that improvements can be made in raising TVA's awareness of fraud prevention and detection. TVA also does not have a formal fraud risk assessment program. Accordingly, we will be working with TVA management to develop and implement more effective controls over fraud.

### **PROGRAM ELEMENTS**

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The following outlines some of the elements of the fraud prevention and detection program we are implementing.

#### **DATA MINING**

We are developing a data mining program, which will use computer analysis and other automated techniques to bring relationships to the surface in large data sets that may assist in identifying (1) errors, (2) irregularities, (3) fraud opportunities, and (4) indicators



of fraud in transactional data. We have hired a forensic analyst, obtained relevant software, and begun running data mining programs. For example, we reviewed TVA's automated credit card records to identify suspicious charges which likely could be personal—e.g, charges to jewelry, toy, sham vendors (who sell products at four or five times market value), and similar stores or internet outlets—and to look for purchasing trends that appear questionable when compared to historical purchases.



### **INTELLIGENCE AND ANALYSIS UNIT**

We have created an Intelligence and Analysis Unit to collect, analyze, and disseminate information on ongoing and/or possible emerging criminal activity affecting TVA, to determine the identities of persons potentially involved in criminal activities, and to assist investigators in understanding complex scenarios and large amounts of seemingly unrelated data. This unit currently is staffed by two investigators. Their functions include closely coordinating with OIG Audits to identify potential areas of fraud and compiling leads from agents across the Valley to identify trends.

### **FRAUD RISK ASSESSMENTS**

We will be working with TVA management to conduct fraud risk assessments throughout TVA. A fraud risk assessment is a process for management and business process owners to identify and analyze fraud risk factors that may be common to general business practices and also specific to the organization and its operations. This process will involve evaluating fraud risk factors, identifying possible fraud schemes and scenarios, prioritizing identified fraud risks, and evaluating whether mitigating controls exist and assessing whether they are effective.

We are sponsoring training on conducting risk assessments and will facilitate assessments in various key business units. We intend for this to be an ongoing process to assist TVA in effectively ensuring there are adequate antifraud controls across all TVA business units.



## Audits

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### Summary of Representative Audits

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Audits are initiated from (1) the OIG annual workplan, (2) additional issues identified by the OIG subsequent to the annual workplan, (3) issues identified by cooperative efforts with TVA management, and (4) concerns raised by TVA management or other stakeholders. During this reporting period, we completed 34 audits which identified almost \$1.8 million in questioned costs and almost \$1.5 million in funds which could be put to better use. In addition, management used the results of our preaward audits in this and prior reporting periods to save \$7.2 million. We also identified numerous opportunities for TVA to improve program operations. Our audits included (1) pre- and postaward contract audits, (2) other financial-related audits, (3) IT reviews, and (4) operational audits.

#### **TVA USES PREAWARD CONTRACT AUDITS TO SAVE ALMOST \$7.2 MILLION**

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During this reporting period, TVA management successfully negotiated almost \$7.2 million in savings as a result of audits issued during this and previous reporting periods. We completed three preaward audits in this reporting period that identified almost \$1.5 million in potential savings opportunities. Highlights of the preaward audits follow.

- We reviewed the cost proposals submitted by two contractors to provide engineering support services. We determined one contractor's proposed cost recovery rates were overstated and estimated TVA would save almost \$1.5 million over the planned 5-year contract term by negotiating a reduction in the rates to eliminate the overstated costs. We determined the second contractor's proposal was fairly stated except for several labor rate ranges. TVA management used our audit results to negotiate better pricing terms with the contractors.
- We assessed the effect on a contractor's indirect cost recovery rates if TVA (1) changed the contractor from staff augmentation services to managed task services and (2) allowed a fringe benefit rate to be added to the contract. TVA management used our audit findings to negotiate new contract rates.





## CONTRACT COMPLIANCE AUDITS IDENTIFY ALMOST \$1.8 MILLION IN QUESTIONED COSTS

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During this reporting period, we completed ten contract compliance-related audits that identified almost \$1.8 million in ineligible and unsupported costs. Management generally agreed with our findings and has taken or plans to take corrective action. Highlights of some of the more significant audits follow.

- We reviewed the costs billed to TVA by a contractor for administration of TVA's preferred provider health plan. We determined TVA had not been paid its share of the contractor's 1999 hospital audit recoveries. The contractor agreed with our finding and refunded \$532,194 to TVA to cover the amount due plus accrued interest. We also determined TVA was due an additional \$63,000 because the contractor had withheld certain fees it was not entitled to. TVA subsequently recovered this amount from the contractor.
- We reviewed four contracts TVA had with a contractor for the purchase of sootblower equipment and replacement parts. We determined TVA had been over-billed about \$246,000 under the two replacement parts contracts because the contractor had not complied with the contract's price change provisions and had used some incorrect unit prices. We also found TVA had inadequate contract documentation for the two equipment contracts which prevented us from expressing an opinion on the costs that had been billed to TVA. TVA management agreed with our findings and plans to (1) recover the overbilled costs and (2) assemble an equipment contract with specific workscope and pricing terms.
- We audited the costs billed by a contractor for providing flue gas desulfurization equipment, related engineering services, and other scrubber related work for TVA's fossil plants. We determined the contractor had billed TVA in accordance with the contract terms except for about \$63,000 related to (1) license fees it had not yet incurred, (2) miscellaneous errors on travel vouchers and time charges, (3) mathematical errors on invoices, and (4) unallowable entertainment expenses.





## Audits

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The contractor provided a \$25,500 credit for the license fees, and TVA management plans to recover the remaining overbillings.

- We reviewed the contract termination claim filed by a subcontractor providing support for TVA's flue gas desulfurization work. We found the subcontractor's claim was not supported by actual costs. TVA management used the results of our audit to negotiate a settlement agreement that saved about \$80,000.
- We reviewed a claim filed by a contractor for the termination of a fixed-price contract it had with TVA for the design and supply of a crystallizer system for the Columbus Regenesys Project. We determined the contractor's claim was overstated by \$82,075 due to unsupported or ineligible (1) direct job costs, (2) initial preparatory costs, (3) closeout costs, and (4) fee. TVA management is negotiating a settlement with the contractor.

### **FINANCIAL-RELATED REVIEWS FIND NO MATERIAL PROBLEMS**

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During this reporting period, we completed five financial-related audits, including two audits of TVA's external auditor's reviews of interim financial information for the second and third quarters of FY 2004. Highlights of the significant audits follow.

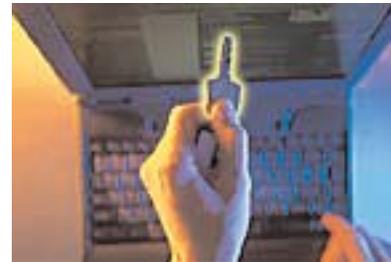
- We determined TVA generally had adequate internal controls over administration of Economic Development loan funds. However, we recommended several process improvements for management's consideration and also recommended 11 loans which are considered uncollectible, totaling \$5.29 million, be written off. TVA management is taking actions to implement our recommendations.
- In two audits related to bond issuance processes, we determined the internal control designs of (1) the bond issue and bond call processes and (2) classifying, recording, and disclosing bond issue and reacquisition costs were adequate to meet TVA's business objectives and legal requirements. We noted, however, that TVA's FY 2003 financial statement disclosure contained an immaterial inaccuracy in that debt issue cost amortization was overstated by \$11,043 for a recalled bond. Management agreed and implemented corrective actions.



- We found no instances where TVA's external auditor's reviews of TVA interim financial information for the second and third quarters of FY 2004 did not comply with Government Auditing Standards in all material respects, including required communications to appropriate parties.

### **TVA'S IT SECURITY PROGRAM MOVES FORWARD**

During this reporting period, we completed six audits in the IT environment, including a review of TVA's progress in complying with federal security requirements. In this review, we found TVA's security program structure is adequate to meet federal requirements, and TVA is making substantial progress in correcting significant security deficiencies.



The remaining five reviews pertained to (1) security at two TVA facilities (a generation plant and a transmission facility), (2) internal controls for TVA's fuels and generation data systems, and (3) access termination processes for TVA's supply chain system. We found improvements were needed to address weaknesses in the following areas:

- Logical security controls designed to prevent unauthorized access to system programs and data. Various weaknesses at the facilities related to communication protocols, system vulnerabilities, security configurations, standard system security, authentication, and access management.
- Physical controls at the facilities designed to prevent security breaches and protect equipment and personnel from hazards.
- Internal controls in the generation data system related to completeness, accuracy, integrity, and usefulness of the data.
- Logical controls within the supply chain system related to access, documentation of access changes, and data accuracy, and within the fuels system related to unit cost calculations and managing user accounts.



## Audits

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TVA management agreed with our findings and either has implemented or is in the process of implementing corrective actions. Some of the corrective actions to address our findings are part of an ongoing agency-wide effort to improve security controls in TVA's existing IT infrastructure.

### **PERFORMANCE REVIEWS**

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#### **IMPROVED PROCEDURES RECOMMENDED FOR TVA'S HOSPITALITY PROGRAM**

We reviewed the TVA hospitality program for FY 2003 to (1) determine the types and level of expenditures for hospitality activities in TVA organizations and (2) assess compliance with policies and procedures related to the hospitality program. TVA believes its hospitality program is necessary and beneficial to its business interests and to its communication with, support of, and recognition of employees. We determined:

- TVA hospitality and special event-related expenditures for FY 2003 totaled almost \$6.5 million.
- TVA's business practice on hospitality afforded TVA employees wide discretion to incur hospitality expenses. Accordingly, we found no instances of noncompliance. However, TVA's practice of allowing TVA employees to engage in hospitality spending without more specific guidance increased the risk of harm to TVA's reputation. TVA's business practice on hospitality was revised by the Board on August 7, 2004, and a memorandum was issued to the TVA Management Committee to provide additional guidance and establish standard guidelines for TVA employees.
- TVA organizations did not accurately classify \$754,281 in expenses in accordance with TVA accounting procedure.

Accordingly, we recommended TVA implement procedures to improve the reporting, reviewing, and monitoring of hospitality expenditures across TVA organizations. In addition, the new procedures should address each line organization's responsibility to appropriately document the justification for significant hospitality expenditures, including a documented reputation risk analysis to ensure the activity would not likely be



perceived by a reasonable member of the public as an improper or inefficient use of TVA resources. Management agreed with our recommendations and has implemented or plans to implement corrective actions.

### **PROCESS IMPROVEMENTS RECOMMENDED FOR FUTURE POWER GENERATION DECISIONS**

Based on information obtained in a FY 2002 survey of TVA's Power Supply Planning (PSP) process, we reviewed the circumstances surrounding TVA's decisions to build and subsequently cancel construction of a 500 megawatt combined-cycle generating plant. We determined that while many factors influenced TVA's build and subsequent cancellation decisions for the plant, those decisions were both consistent with and reasonably supported by PSP data. However, we noted various circumstances that warranted consideration of process improvements in future power generation decisions. Accordingly, we recommended TVA (1) consider incorporating more risk management techniques into the PSP process and (2) integrate the processes used by the various organizations that contribute to PSP decision making to achieve more timely, systematic scenario analyses. Management agreed with our recommendations and has taken or plans to take actions to improve the process.

### **IMPROVEMENTS IN COMPLIANCE WITH HEARING CONSERVATION PROGRAM (HCP) RECOMMENDED**

TVA hearing loss claims have risen from \$1.1 million in FY 1997 to \$8.7 million in FY 2002. TVA established the HCP "to prevent employee hearing loss from exposure to high noise levels." Our review of TVA's HCP determined the HCP complied with Occupational Safety and Health Administration regulations. However, in assessing compliance with TVA's own HCP, we noted (1) TVA had not identified and documented employees who should be included in the HCP; (2) TVA had not performed personal noise sampling representative of its workforce at some sites; (3) TVA did not have valid sound level survey information for identifying high noise levels at some plants; (4) TVA had not promulgated sufficient guidance regarding when dual hearing protection is required; and (5) some TVA sites had not provided an appropriate variety of earplugs for employees' use. Additionally, TVA was not identifying some employees who have



experienced significant hearing loss. Management agreed with our recommendations and has taken or plans to take appropriate corrective actions.

### **IMPROVEMENTS IN PUBLIC POWER INSTITUTE (PPI) PROGRAM MEASURES RECOMMENDED**

TVA established the PPI to help fulfill its commitment to protect natural resources and



the environment while working to provide low-cost, reliable power by collaborating with others to develop, demonstrate, and deploy new energy-related technologies. Our review determined that (1) PPI's performance measures do not include a majority of the work performed and (2) cost benefit measures should be improved. We also found duplication in the work

performed by PPI and another TVA organization, and opportunity for improvements in risk management techniques.

Accordingly, we recommended TVA (1) evaluate ways to improve program measures through benchmarking and cost-benefit analysis, (2) continue efforts to consolidate the PPI and the other TVA program, and (3) implement risk-management strategies when pursuing large-scale research and development projects. Management agreed with our recommendations and has taken or plans to take actions to improve the process.

### **NO MATERIAL ERRORS FOUND IN DEPARTMENT OF LABOR (DOL) WORKERS' COMPENSATION PAYMENTS**

TVA's Workers' Compensation Department helps prevent improper benefits and reduces costs by validating charges received from the DOL Office of Workers' Compensation Program (OWCP). Our review of the accuracy of the DOL billings to TVA for approximately \$60.5 million in workers' compensation claims identified \$7,886 in overpayments which consisted of one incorrectly calculated schedule award and two duplicate disability payments. We also recommended management determine whether additional verification of DOL billings would be cost effective. Management agreed to



seek recovery of the identified overpayments and evaluate the appropriate extent of monitoring.

### **TVA'S CONCERNS RESOLUTION PROGRAM (CRP) WORKING**

TVA's CRP was designed to help ensure all TVA and contractor employees supporting TVA Nuclear (TVAN) "are free to express safety issues, concerns, or differing views to TVAN management without fear of reprisal and all such concerns and issues are investigated and resolved in a timely manner." We performed three separate audits which assessed the willingness of TVA employees and contractors to report nuclear safety and quality issues through various avenues, including TVA's CRP. The scope of the three reviews corresponded to the (1) TVAN workforce, employees and contractors with unescorted access to TVA's nuclear facilities; (2) BFN Unit 1 restart project contractors; and (3) Sequoyah Nuclear Plant (SQN) employees and contractors.

Overall, we determined the TVAN workforce and contractors at BFN Unit 1 and SQN generally felt free to raise nuclear safety and quality issues through some avenue.



## Investigations

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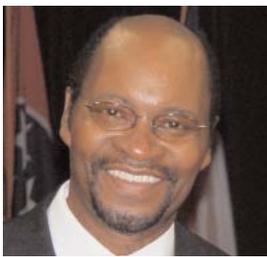
### Summary of Representative Investigations

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During the past six months, we closed 163 investigations based, in part, on allegations and concerns received from ratepayers, TVA management and employees, governmental and congressional staffs, and OIG auditors. Our investigations, including task force projects, resulted in (1) over \$1.3 million in recoveries, projected savings, and fines/penalties; (2) nine subjects indicted; and (3) three subjects convicted. Below we discuss the President's Council on Integrity and Efficiency (PCIE) award for and retirement of the Assistant Inspector General for Investigations, results of our peer review, and illustrative cases.

#### **RETIRING ASSISTANT INSPECTOR GENERAL, INVESTIGATIONS, RECEIVED PCIE AWARD**

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G. Donald Hickman, the Assistant Inspector General for Investigations for the past ten years, has retired. Shortly before he retired, we learned that Mr. Hickman was being recognized by his peers for his accomplishments. The PCIE has chosen Mr. Hickman to receive an Individual Accomplishment Award for his outstanding effort and persistence in the development and implementation of a federal OIG investigation peer review process, resulting in enhanced quality and credibility of all OIG Investigation units. This is the second individual award given to Mr. Hickman by the IG community—in 2000 he received an Award of Excellence from the Executive Council on Integrity and Efficiency for his leadership and sustained contributions to the law enforcement community. His contributions to the office will be missed.

#### **PEER REVIEW COMPLETED**

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The Department of Commerce Office of the Inspector General conducted a peer review of our Investigations organization in accordance with the guidance issued by the PCIE. (Each OIG with statutory law enforcement authority under the IG Act will undergo a peer review every three years.)



On July 27, 2004, the Department of Commerce Inspector General issued a final report finding the TVA OIG was in “full compliance,” the highest possible rating. More specifically, that report concluded our system of internal safeguards and management procedures in effect for the year ended February 1, 2004, was in full compliance with the quality standards established by the PCIE and the United States Attorney General’s Guidelines, and those safeguards and procedures provided reasonable assurance that we are conforming with professional standards in the conduct of our investigations.

In a separate letter, also dated July 27, 2004, the Department of Commerce Inspector General cited two noteworthy accomplishments. The noteworthy accomplishments were that our system of documenting subject interviews included some innovative methods, and we had an outstanding system for maintaining, updating, and documenting agent training.

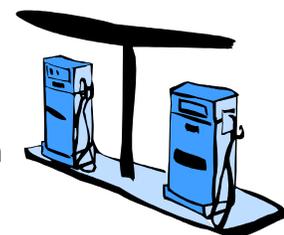
## ILLUSTRATIVE CASES

Our cases during the past six months included fraud against TVA by TVA employees, contractor employees, and workers’ compensation beneficiaries. We also closed several cases involving coal purchases which helped TVA save over \$400,000, and we continued our support of various joint task forces. The following is a brief summary of illustrative cases.

### FRAUD

Cases involving fraud by TVA employees and contractor employees included the following. (Three other cases were reported under the Special Features section about BFN Unit 1 restart.)

- A Transmission/Power Supply foreman misused his Wright Express (WEX) credit card provided in TVA vehicles to purchase gasoline. The foreman used the WEX card to put gas in cars belonging to friends and people he did not know. He would double the amount of gas a person wanted in exchange for cash, i.e., the person paid him \$10 cash in exchange for \$20 in gas on the WEX card. He used several





## Investigations

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different WEX cards at various service stations in the Knoxville area. The amount of TVA's loss was approximately \$45,000. TVA terminated the foreman, who was indicted by a federal grand jury on June 16, 2004, and subsequently pled guilty.

- A TVA employee used her government travel card (1) for personal expenses, including over \$14,000 in cash advances, in violation of TVA policy; (2) to purchase airline tickets costing over \$3,000 for personal travel for herself and other non-TVA employees where those tickets were direct-billed to TVA; and (3) to rent cars for personal use where those rental charges were direct-billed to TVA. In addition, she misused leave. The employee resigned during our investigation, and the matter was referred for prosecutive consideration.



- A Fossil Power Group employee used his TVA travel card for personal charges, including three travel charges that were direct-billed to TVA. The employee reimbursed TVA for the personal expenses and was suspended for 14 days.
- During July 2004, a contract employee was indicted by a federal grand jury in the Northern District of Alabama on two counts of making false statements. The contractor submitted false statements in order to receive approximately \$50,000 in per diem over a three-year period.
- A former contract employee entered TVA facilities after being terminated and submitted eight timesheets for payment. The contractor, not knowing the timesheets were false, paid the former employee and passed the cost to TVA. On May 6, 2004, the former employee pled guilty in state court to theft. He was granted pre-trial diversion and placed on unsupervised probation for one year. He made restitution to TVA in the amount of \$5,344.



### WORKERS' COMPENSATION CASES

We had two reportable workers' compensation cases during this period.

- In one case, a former TVA ironworker was indicted on four counts of making false statements to OWCP to receive workers' compensation benefits to which he was not entitled. Our investigation showed the employee did not report that he derived income from operating an auto salvage business.
- In the other investigation, we found a fossil plant worker filed a false workers' compensation claim. The worker, who claimed he was injured at work, admitted during an interview that he was in fact injured at home. Management terminated the employee, and the matter was referred for prosecutive consideration.



### COAL CASES

Coal cases closed during this reporting period helped TVA save over \$400,000, as follows.

- We investigated an anonymous tip that a TVA coal contractor was manipulating coal samples for coal shipped to TVA. Train shipments were diverted, sampled, and tested by TVA. The testing identified coal quality problems. Subsequently, the contractor proposed using the coal as feedstock for synfuel. TVA management accepted the proposal which resulted in a gross savings of more than \$442,000. The coal contractor also was penalized \$14,037 for one train that did not meet coal quality specifications.



## Investigations

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- TVA management discovered discrepancies between the Coal Quality Adjustment Reports (CQAR) at a fossil plant prepared by TVA and the vendor. Based on these discrepancies, a camera was installed and a TVA employee was videotaped not



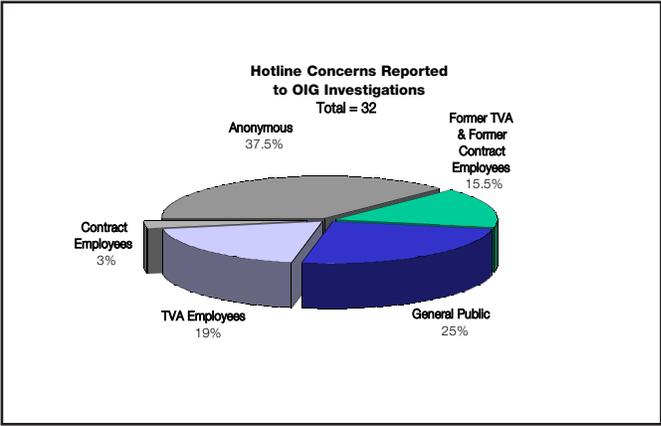
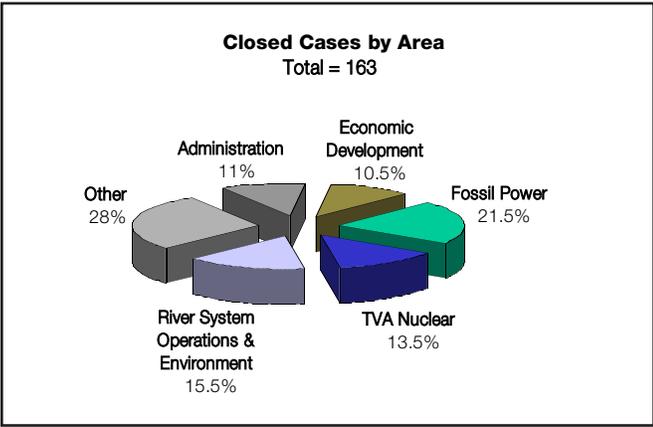
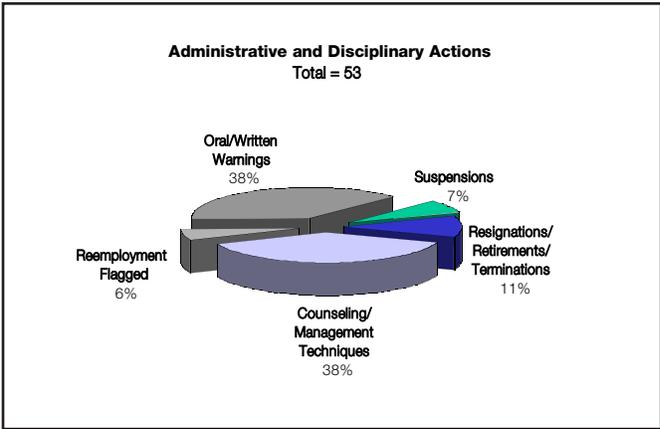
properly preparing the coal samples. The improperly prepared samples prevented accurate calculation of the CQAR, costing TVA an estimated \$53,000 to \$200,000. The employee retired upon learning he was under investigation. Prosecution was declined

because the employee had not been required to certify preparation of the coal samples. TVA management is considering our recommendations to prevent recurrence of this type situation.

### TASK FORCES

We continued our support of task forces on health care fraud, environmental crimes, and terrorism. During this reporting period, as a result of task force activities, an Indiana based firm that manufactures trailers for the trucking industry pled guilty in federal court to two counts of violating the Clean Water Act. The company acknowledged dumping more than 120,000 gallons of a caustic solution in a Scott County, Tennessee, waterway, causing two children to suffer chemical burns. As part of the plea agreement, the company agreed to pay a total of \$400,000. The investigation was conducted by the Environmental Crimes Joint Task Force (ECJTF), which is comprised of members from numerous federal and state agencies.

In another ECJTF case, the defendant company pled guilty to a misdemeanor charge for releasing diesel fuel from its pipeline into waters of the United States without a permit. The diesel fuel was discharged when a pipe ruptured. The defendant remediated the site and agreed to pay a \$50,000 fine and \$350,000 in restitution for environmental education and protection and incident response training and equipment.





### Summary of Representative Inspections

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Inspections may be initiated from various sources including: (1) annual project planning, (2) management requests, (3) audit/investigative referrals, and (4) spin-off reviews resulting from an ongoing inspection. During this reporting period, we completed eight inspections which identified over \$226,000 in cost savings and opportunities for TVA to improve program operations.

#### **CONTRACT INSPECTIONS IDENTIFY OVER \$226,000 IN COST SAVINGS**

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During this reporting period, we completed six contract-related inspections which identified over \$226,000 in cost savings and opportunities to improve controls. Management generally agreed with our findings and has taken or plans to take corrective action. Highlights of some significant inspections follow.

- An ammonia supplier requested a price increase citing increased freight costs. TVA management approved the increase on a provisional basis pending the results of our review. Our review determined the supplier did not directly incur additional freight costs and could not support the requested increase. In addition, we identified overbillings of \$204,229 of which over \$77,000 was related to billings for additional freight costs that were not incurred by the supplier and about \$127,000 in other various billing errors. TVA management agreed with the findings and has taken action to recover the overbilled costs.
- We determined an energy right® contractor engaged in various improper schemes against third parties and TVA's energy right® Heat Pump Plan/Financing Program,



which resulted in \$22,500 in improper claims. We also (1) found the contractor's actions were inconsistent with program objectives and did not comply with program requirements, and (2) identified numerous opportunities for improvement in internal controls over implementation of the program and in the written policies. TVA management agreed with the findings, identified appropriate corrective actions, and withheld payment for the fraudulent claims.



## **GOVERNMENT TRAVEL CARD CONTROLS COULD BE IMPROVED**

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We reviewed controls related to government travel cards assigned to TVA employees for official travel-related expenses. Certain charges (airline and rental car) are directly billed to TVA and shown on the credit card statement as a memo item, while the employee must pay the remaining charges and request reimbursement from TVA. Our inspection disclosed controls could be improved by (1) developing more detailed policies and procedures, (2) implementing a salary offset policy to reduce the costs associated with charged off accounts, (3) providing direct-charge training for employees, (4) reinforcing management's responsibility to review credit card direct charges, and (5) periodically reevaluating credit limits for appropriateness. TVA management agreed to implement all the recommendations.



## Legislation and Regulations

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During this reporting period, legislative areas of interest included matters pertaining to the IG community and TVA. We also established a new Assistant Inspector General for Administration and Government Relations position to better focus our efforts in this area. As noted earlier in this report, Ronald Wise is our first AIGAGR. His duties will include developing working relationships with congressional members and ensuring we keep them informed of our activities and are responsive to their concerns.

### THE IG COMMUNITY

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The TVA IG, Richard W. Moore, serves on the Legislation Committee for the PCIE. The overall mission of this Committee is to ensure the PCIE is kept abreast of congressional matters of interest to the IG community as a whole or which may impact OIG statutory authority, duties, and organization. The Committee also develops, coordinates, and represents to Congress official PCIE positions on particular legislative issues. Finally, the Committee serves as a resource base for the IG community on congressional rules, operation, and procedures. We shall continue to follow legislative items of interest to the IG community and work with the PCIE in keeping Congress apprised of our views on those matters.

### TVA

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We continued to follow issues of interest to TVA, including federal energy legislation which included a provision to restructure the TVA Board. We believe the pros and cons of this proposed legislation are being fully explored, and look forward to working with both TVA and Congress in these matters. We also responded to requests for information from members of Congress and their staffs.



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# APPENDICES

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## Appendix 1

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### Index of Reporting Requirements Under the Inspector General Act

REPORTING REQUIREMENT	PAGE
Section 4(a)(2) Review of Legislation and Regulations	31
Section 5(a)(1) Significant Problems, Abuses, and Deficiencies	10-30
Section 5(a)(2) Recommendations With Respect to Significant Problems, Abuses, and Deficiencies	10-30
Section 5(a)(3) Recommendations Described in Previous Semiannual Reports on Which Corrective Action Has Not Been Completed	Appendix 4
Section 5(a)(4) Matters Referred to Prosecutive Authorities and the Prosecutions and Convictions That Have Resulted	Appendix 5
Section 5(a)(5) and 6(b)(2) Summary of Instances Where Information Was Refused	None
Section 5(a)(6) Listing of Audit Reports	Appendix 2
Section 5(a)(7) Summary of Particularly Significant Reports	10-30
Section 5(a)(8) Status of Management Decisions for Audit Reports Containing Questioned Costs	Appendix 3
Section 5(a)(9) Status of Management Decisions for Audit Reports Containing Recommendations That Funds Be Put to Better Use	Appendix 3
Section 5(a)(10) Summary of Unresolved Audit Reports Issued Prior to the Beginning of the Reporting Period	None
Section 5(a)(11) Significant Revised Management Decisions	None
Section 5(a)(12) Significant Management Decisions With Which the Inspector General Disagreed	None
Section 5(a)(13) Information under Federal Financial Management Improvement Act of 1996	None



## Audit Reports Issued

AUDIT REPORT NUMBER AND DATE	TITLE	QUESTIONED COSTS	UNSUPPORTED COSTS	FUNDS PUT TO BETTER USE
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### CONTRACT

<b>2004-024C</b> 04/28/04	Washington Group			\$1,471,000
<b>2004-025C</b> 04/28/04	MESA			
<b>2004-041C</b> 05/28/04	Midpoint International - Review of Statutory Payments			
<b>2003-036C-02</b> 06/04/04	Diamond Power - Cost Compliance			
<b>2003-037C</b> 06/04/04	Blue Cross Blue Shield of Tennessee	\$595,290		
<b>2003-036C-01</b> 06/21/04	Diamond Power - Cost Compliance	246,734		
<b>2004-033C</b> 06/30/04	Audit of G-UB-MK Subcontract No. 1999-001 with Williams Specialty Services			
<b>2003-062C</b> 07/12/04	GTSI Corporation	566		
<b>2004-043C</b> 08/13/04	National Inspection & Consultants, Inc. - Preaward Audit			
<b>2004-052C</b> 09/10/04	Philadelphia Mixing Solutions - Termination Claim	165,090		
<b>2004-032C</b> 09/20/04	Advatech LLC - Contract No. 18244 - Flue Gas Desulfurization Projects	63,122		
<b>2004-057C</b> 09/20/04	Swenson Technology, Inc. - Limited Review of Cost for Contract Termination	82,075	\$8,965	
<b>2004-003C-01</b> 09/27/04	Bechtel Power Corporation Engineers-Constructors - Contracts 8471	602,611	94,069	



## Appendix 2

### Audit Reports Issued

AUDIT REPORT NUMBER AND DATE	TITLE	QUESTIONED COSTS	UNSUPPORTED COSTS	FUNDS PUT TO BETTER USE
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#### FINANCIAL

**2004-035F**

05/14/04	Audit of PriceWaterhouse Cooper's Review of TVA's 2nd Quarter, FY 2004 Financial Information			
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**2003-053F-01**

06/03/04	Assess Controls for Generation Data in Operations Data Store System and Web Based Data Entry Page			
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**2004-031F**

07/19/04	Bond Offering Circular			
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**2004-046F**

08/16/04	Audit of PriceWaterhouse Cooper's Review of TVA's 3rd Quarter, FY 2004 Financial Information			
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**2004-050F**

08/18/04	Assess Controls Over Classification, Recording, and Disclosing Debt Issue and Reacquisition Costs			
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#### INFORMATION TECHNOLOGY

**2004-013T**

05/20/04	Fossil Plant IT Security			
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**2003-053F-02**

06/03/04	Operations Data Store Logical Security Controls			
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**2003-056T**

06/10/04	Pre-Implementation Review of TVA's New Fuelworx Application			
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**2004-004T**

07/28/04	Operations Center IT Security			
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**2004-049T**

09/13/04	Timeliness of Terminating Passport Access			
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**2004-045T**

09/16/04	Federal Information Security Management Act Evaluation			
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## Audit Reports Issued

AUDIT REPORT NUMBER AND DATE	TITLE	QUESTIONED COSTS	UNSUPPORTED COSTS	FUNDS PUT TO BETTER USE
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### PERFORMANCE

<b>2003-043P</b> 04/21/04	TVA's Hearing Conservation Program			
<b>2003-009P</b> 06/25/04	Franklin County Combined Cycle Project			
<b>2004-040F</b> 07/01/04	Verification of TVA's Compliance With the Green Pricing Accreditation Program Requirements for Calendar Year 2003			
<b>2004-006F</b> 07/13/04	Review of Public Power Institute Performance			
<b>2004-010P</b> 08/11/04	Review of TVA's Workers' Compensation Claims Process	\$7,886		
<b>2004-038F</b> 08/16/04	Concerns Resolution Program - Browns Ferry Nuclear Plant Unit 1 Restart			
<b>2004-036F</b> 08/17/04	Concerns Resolution Program - TVA Nuclear 2004			
<b>2004-037F</b> 08/24/04	Concerns Resolution Program - Sequoyah Nuclear Plant 2004			
<b>2004-011F</b> 09/27/04	Effectiveness of TVA's Economic Development Loan Fund			
<b>2004-014F</b> 09/28/04	TVA's Hospitality Expenses			
<b>TOTAL</b>	<b>34</b>	<b>\$1,763,374</b>	<b>\$103,034</b>	<b>\$1,471,000</b>



## Appendix 3

### Audit Reports Issued With Questioned Costs

	NUMBER	QUESTIONED COSTS	
		TOTAL	UNSUPPORTED
A. For which no management decision has been made by the commencement of the reporting period	3	\$3,361,621	\$343,898
B. Which were issued during the reporting period	8	\$1,763,374	\$103,034
<b>Subtotals of A and B</b>	<b>11*</b>	<b>\$5,124,995</b>	<b>\$446,932</b>
C. For which a management decision was made during the reporting period	9	\$4,388,578	\$343,898
(i) Dollar value of disallowed costs	9	\$2,948,469	\$314,938
(ii) Dollar value of costs not disallowed	3	\$1,440,109	\$28,960
D. For which no management decision has been made by the end of the reporting period	3	\$736,417	\$103,034
E. For which no management decision was made within six months of issuance	0	\$0	\$0

\* The total number of reports (A+B) differs from the sum of C and D when the same reports contain recommendations with and without management decisions.



## Audit Reports Issued With Recommendations for Better Use of Funds

	NUMBER	DOLLAR VALUE
A. For which no management decision has been made by the commencement of the reporting period	2	\$6,103,800
B. Which were issued during the reporting period	1	\$1,471,000
<b>Subtotals of A and B</b>	<b>3</b>	<b>\$7,574,800</b>
C. For which a management decision was made during the reporting period	3	\$7,574,800
(i) Dollar value of costs agreed to by management	3	\$7,021,180
(ii) Dollar value of costs not agreed to by management	1	\$553,620
D. For which no management decision has been made by the end of the reporting period	0	\$0
E. For which no management decision was made within six months of issuance	0	\$0



## Appendix 4

### Audit Reports With Corrective Actions Pending

Final corrective actions on recommendations in five contract compliance audits, two operational audits, three financial audits, and nine IT audits have not been fully implemented; however, all are being implemented in accordance with currently established milestones.

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**AUDIT REPORT  
NUMBER  
AND DATE****DESCRIPTION**

<b>2001-064T</b> 12/21/01	<b>Hydro Automation Security-HDCC</b> This report contained recommendations regarding physical and logical security of the Hydro Dispatch Control Cell. TVA completed final action on October 12, 2004.
<b>2001-074T</b> 01/07/02	<b>Application Review of Pegasys</b> This report contained recommendations regarding facility access control. TVA is reevaluating options for addressing these recommendations.
<b>2002-012T-01</b> 10/25/02	<b>Security Review of Nuclear Facility Access Control Systems-SQN</b> This report contained recommendations regarding facility access control. TVA plans to complete final action by January 2005.
<b>2002-017T</b> 06/25/02	<b>Hydro Automation-Dams</b> This report included recommendations regarding the physical and logical security of hydro automation systems at seven hydroelectric facilities. TVA completed final action on October 12, 2004.
<b>2002-025T</b> 08/07/02	<b>Security of Windows 2000/Windows XP</b> This report contained recommendations to strengthen environmental and logical controls of TVA's implementation of Windows 2000 and Windows XP. TVA management plans to complete final action by February 2005.
<b>2002-075E</b> 03/03/03	<b>Integrity of Selected Fossil Power Data Used in TVA's Energy Trading Model</b> This report included recommendations to improve the integrity of selected fossil data used in TVA's energy trading decision support model. TVA management plans to complete final action by May 2005.
<b>2003-003C</b> 06/17/03	<b>Page Clearing Contractors</b> This report included recommendations to recover ineligible costs. TVA management has reached a settlement agreement with the contractor and is receiving monthly credits for costs determined to have been disallowed. The remaining balance should be collected by December 31, 2004.
<b>2003-004C</b> 03/30/04	<b>A &amp; G Tree Service, Inc.</b> This report included recommendations to (1) recover unsupported costs and (2) require the contractor to compensate its employees for underpaid wages. TVA management plans to recover any overbilled costs. Also, TVA is reviewing prevailing wage rates for right-of-way clearing contractors and plans to have this completed by December 31, 2004.
<b>2003-015F</b> 07/28/03	<b>Review of Completed Plant Retirements</b> This report contained recommendations to correct completed plant retirement inaccuracies, improve accounting for completed plant retirements, and strengthen management's controls over retirements processing. TVA management agreed to implement most of our recommendations and expects to complete final action by December 31, 2004.



## Audit Reports With Corrective Actions Pending

AUDIT REPORT  
NUMBER  
AND DATE

DESCRIPTION

<p><b>2003-019F-04</b> 01/29/04</p>	<p><b>TVAN Overhead Recovery</b> This report contained recommendations to ensure TVAN's (1) organizational overhead rate for external business is calculated on an annual basis, (2) labor markup rate for external business includes fringe benefits and indirect labor costs, (3) fringe benefit rate for internal services charged to external business is adjusted to reflect the estimated straight-time labor component, and (4) overhead rates are applied to external business costs in a manner consistent with the rate calculation method. TVA management agreed to implement our recommendations and is currently working on the process for accurate calculation and proper application of indirect cost recovery rates.</p>
<p><b>2003-024F</b> 11/18/03</p>	<p><b>Review of TVA's Accounts Receivable and the Allowance for Doubtful Accounts</b> This report contained recommendations to (1) develop, document, and implement guidelines for estimating the allowance for doubtful accounts, (2) ensure reconciliation of the general ledger and subsidiary accounts include documentation of corrections and adjustments made during power and nonpower reconciliations and management review and approval of all nonpower adjusting journal entries, (3) make modifications to the write-off process to ensure invoices are written off in a timely manner, (4) develop and implement procedures to track written-off accounts for future collection efforts or business decisions, (5) ensure accounts are written off in accordance with policy, and (6) review and update Accounting Procedure 25 to clarify the criteria for referring past due customers to the Office of General Counsel. TVA management agreed to implement our recommendations and has transitioned the responsibilities to a new group. Processes and procedures will be evaluated and updated in FY 2005, and a new system is planned.</p>
<p><b>2003-044F</b> 01/29/04</p>	<p><b>Tritium Program - Department of Energy (DOE) and TVA Interagency Agreement No. DE AI02 00DP00315</b> This report contained a recommendation that DOE and TVA take appropriate corrective actions to ensure that TVA's costs are fully reimbursed as required by the interagency agreement and the Economy Act. TVA management agreed with our recommendations and began proper application of improved overhead rates. TVA management intends to consider all of the adjustment amounts when certain fixed payments by DOE to TVA related to foreign equipment are discussed in FY 2010.</p>
<p><b>2003-045C</b> 12/02/03</p>	<p><b>Three Rivers Contracting</b> This report included recommendations to require the contractor to (1) establish appropriate documentation and approval processes and (2) compensate its employees for underpaid wages. TVA management has required the contractor to implement documentation standards. Also, TVA is reviewing prevailing wage rates for right-of-way clearing contractors and plans to have this completed by December 31, 2004.</p>
<p><b>2003-046C</b> 12/02/03</p>	<p><b>Southeastern Construction &amp; Equipment Company, LLC</b> This report included recommendations to recover ineligible costs. TVA management is working with the Office of General Counsel relative to options available for recovery since TVA has not had a contractual relationship with the contractor since July 2003, and there are no accounts payable available to withhold funds due TVA.</p>
<p><b>2003-049T</b> 11/18/03</p>	<p><b>Bill Out Subsystem</b> This report included a recommendation to ensure adequate annual disaster recovery testing. TVA management is implementing corrective action with an expected completion date of September 2005.</p>



## Appendix 4

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### Audit Reports With Corrective Actions Pending

AUDIT REPORT  
NUMBER  
AND DATE

DESCRIPTION

**2003-054T**  
11/13/03

**Hydro Plant IT Security**

This report included recommendations to strengthen logical, physical, and management controls over IT assets at a hydroelectric facility. TVA management has completed a site emergency response plan and addressed safety issues. Additional efforts are in progress to mitigate remaining control weaknesses with an expected completion date of December 2006.

**2003-067P**  
02/02/04

**TVA's Compliance With the National Energy Conservation Policy Act**

This report contained recommendations to continue to evaluate opportunities to reduce energy consumption including (1) promoting sustainable building design when appropriate and (2) determining whether TVA can implement energy reduction requirements in a lease of TVA space to a private company. Management actions should be completed by early FY 2005.

**2003-068T**  
01/22/04

**Substation IT Security**

This report included recommendations to strengthen logical, physical, and management controls over IT assets at a substation facility. TVA management is implementing planned remediation actions, with completion targeted for December 2006.

**2004-007T**  
01/26/04

**Fossil Plant DCS IT Security**

This report included recommendations to strengthen logical and physical controls over control systems at a fossil generation facility. TVA management is implementing planned remediation actions which are expected to be completed by December 2006.



## Investigative Referrals and Prosecutive Results\*

### Referrals

Subjects Referred to U.S. Attorneys	20
Subjects Referred to State/Local Authorities	5

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### Results

Subjects Indicted	9
Subjects Convicted	3
Referrals Declined	12

\* These numbers include task force activities.



## Highlights

	SEPT 30, 2004	MAR 31, 2004	SEPT 30, 2003	MAR 31, 2003	SEPT 30, 2002
ANNUAL BUDGET (In Millions of Dollars)	\$8.8	\$8.8	\$8.5	\$8.5	\$8.0
CURRENT STAFFING	82	78	78	84	87

### AUDITS

#### AUDITS IN PROGRESS

Carried Forward	29*	37	38	35*	33
Started	38	36	41	41	44
Canceled	(5)	(5)	(8)	(4)	(4)
Completed	(34)	(39)	(34)	(34)	(40)
In Progress at End of Reporting Period	28	29	37	38	33

#### AUDIT RESULTS (Thousands)

Questioned Costs	\$1,763	\$14,127	\$1,908	\$1,125	\$3,816
Disallowed by TVA	2,948	10,453	137	989	911
Recovered by TVA	1,113	697	3,499	221	387

Funds to Be Put to Better Use	\$1,471	\$11,904	\$6,951	\$34,755	\$52,037
Agreed to by TVA	7,021	5,800	6,551	37,969	44,944
Realized by TVA	7,196	11,708	0	38,172	16,014

#### OTHER AUDIT-RELATED PROJECTS

Completed	8	30	15	36	16
Cost Savings Identified/Realized (Thousands)	\$0	0	0	0	0

### INVESTIGATIONS \*\*

#### INVESTIGATION CASELOAD

Opened	118	162	100	87	78
Closed	163	76	92	75	89
In Progress at End of Reporting Period	176	221	135	127	115

#### INVESTIGATIVE RESULTS (Thousands)

Recoveries	\$460	\$3,412	\$100	\$879	\$961
Savings	447.7	863	875	366	8
Fines/Penalties	451.6	10	421	56	86

#### ADMINISTRATIVE AND DISCIPLINARY ACTIONS

Recommended (# of Cases)	14	8	21	15	18
Actions Taken (# of Subjects)	30	75	24	16	7
Counseling/Management Techniques Employed (# of Cases)	16	13	21	16	24

#### PROSECUTIVE ACTIVITIES (# of Subjects)

Referred	25	17	63	12	19
Indicted	9	3	4	6	9
Convicted	3	3	10	4	4

### INSPECTIONS

Completed	8
Cost Savings Identified/Realized (Thousands)	\$226

\* Adjusted from previous reporting period.

\*\* These numbers include task force activities.

Tennessee Valley Authority  
Office of the Inspector General

# Help Track Down Fraud, Waste, and Abuse at TVA



Contact the OIG Hotline  
**1-800-323-3835**

**To report:**

- Contract or computer fraud
- Computer misuse or crimes
- False statements or false claims
- Irregularities in financial reporting
- Conflicts of interest and other ethics violations
- Travel fraud
- Theft or misuse of TVA property
- Management reprisal
- Workers' compensation fraud
- Bribery, kickbacks, or gratuities
- Health care fraud
- Environmental, health, and safety violations

For additional information, see our Web site at [oig.tva.gov](http://oig.tva.gov)

**Promoting**



**Excellence**

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